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No. 92-747

In The

Supreme Court of the United States

October Term, 1992

Wm. F. McCOLLOUGH, et ux.,

Petitioners,

v.

A.G. EDWARDS & SONS, INC.,

Respondent.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. When an unsuccessful party in a securities arbitration failed to request a Statement of Reasons as required by New York Stock Exchange rules, does a District Court have authority to vacate the award for "undue means" as defined in Title 9 U.S.C. § 10(a)(1)?

2. Where a speculative trading, margin account customer incurred significant stock losses on October 19, 1987, defaulted on a promissory note and was unsuccessful in an arbitration, does a District Court have authority to presume error and vacate an arbitration award under Title 9 U.S.C. § 10(a)(1) because it does not contain a statement of reasons?

3. Can an arbitration award be vacated where no evidence exists of fraud or misconduct or to indicate a sophisticated panel considered allegedly improper defenses raised at the commencement of the proceedings (subsequently briefed and argued by counsel), and the award contains no irregularities?

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BRIEF IN OPPOSITION

Respondent A.G. Edwards & Sons, Inc. requests the Court deny the Petition for a Writ of Certiorari to review the judgment of the Ninth Circuit Court of Appeals. The Ninth Circuit Court has correctly applied federal law regarding the scope of judicial review of an arbitration award, where the arbitrators followed applicable arbitration procedures, no evidence of fraud or misconduct exists and the award is proper on its face. The facts and law in this case do not justify exercise of this Court's discretion to grant Certiorari pursuant to U.S. Supreme Court Rule 10.

RESPONDENT'S STATEMENT OF THE CASE

Pursuant to Rule 15 of the Rules of the Supreme Court of the United States, Respondent will address misstatements of fact it its statement of the case. Petitioners Mr. and Mrs. McCollough ("McColloughs") are sophisticated investors who engaged in speculative trading. The McColloughs' Petition mischaracterizes them as unsophisticated investors whose only concern was for safety of investment. Petition at 3. Mr. McCollough was a "real estate speculator" who had twenty years previous investment experience in stocks and bonds. Testimony of Richard Anderson, Ex. B. to Statement of Facts in Support of Plaintiff's Opposition to Motion to Vacate ("Statement of Facts") (E.R. 000124); Tab 1 to Motion to Vacate Arbitration Award (E.R. 000026).[1] McColloughs' counsel admits their sophistication could have been one legitimate basis for the Arbitrators' decision. Transcript of Oral Argument at 25-26.

A. McColloughs' Trading Account

The McColloughs' 1985 and 1986 accounts at A.G. Edwards & Sons[2] ("A.G. Edwards") were options accounts. Exhibit A to Statement of Facts (E.R. 000119-22).

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[1] "ER" refers to Appellant's Excerpt of Record. The record before the District Court consisted of exhibits filed with the parties' motions, responses, and replies that have been provided in the Excerpt of Record because they have independent legal significance. All references to testimony reflect portions of the arbitration transcript that were provided to the District Court in the form of exhibits.

[2] Pursuant to U.S. Supreme Court Rule 29.1, Respondent A.G. Edwards & Sons, Inc. states it is a wholly-owned subsidiary of A.G. Edwards, Inc.

Option accounts are by nature speculative investments. The option agreement, signed by the McColloughs, acknowledges the risks:

> I understand the risks and obligations attached to the various types of options contracts and the various types of transactions that may be made in options. I have evaluated and am capable of bearing the financial risks involved and have determined that trading in options is appropriate to my investment objectives.

Exhibit A to Statement of Facts (E.R. 000119) (dated Jan. 14, 1986). The McColloughs earned a profit of $160,000 in 1986 from speculative option trading, prior to the October 19, 1987 stock market crash. Testimony of William McCollough, Ex. B to Statement of Facts (E.R. 000128-000131).

B. McColloughs Selected Arbitration

The McColloughs complain that they had no choice in the decision to arbitrate *vis-à-vis* other judicial remedies. Petition at 4, 7, 20. After the stock market crash of October 19, 1987, the McColloughs lost the equity position in their account and incurred a debit balance of approximately $250,000. Memorandum and Order at 1-2 (E.R. 000241-000242).

When the McColloughs were unable to satisfy the debit balance, A.G. Edwards agreed to forego legal action in exchange for a promissory note for deferred payments and a release from the McColloughs. Testimony of David Minnick, Ex. B to Statement of Facts (E.R. 000134-000138). The McColloughs made initial payments under the promissory note and then stopped. Memorandum and Order at 2 (E.R. 000242).

After the McColloughs defaulted, A.G. Edwards initiated suit in the United States District Court for the District of Arizona (CIV 88-1731 PHX-EHC). Statement of Facts at 2-3, ¶ 7 (E.R. 000115-000116), Ex. C to Statement of Facts (E.R. 000144-000146). The suit was dismissed upon agreement to arbitrate before the New York Stock Exchange, Inc. ("N.Y.S.E."). *Id.* The McColloughs had retained counsel and submitted a Statement of Claim pursuant to an N.Y.S.E. Uniform Submission Agreement where they acknowledged they would be bound by all applicable N.Y.S.E. Rules on October 14, 1988, and arbitration proceedings were subsequently held. *See* Appendix A; Memorandum and Order at 2 (E.R. 000242).

The sophisticated arbitration panel consisted of three members, two of whom were attorneys. Mr. Parker was a retired executive with Mountain Bell who had a bachelors degree from Occidental College in Los Angeles, and had studied graduate level work at Dartmouth College and Arizona State University. Exhibit F to Statement of Facts (E.R. 000211-000218).

The second arbitrator, Charles Lehing, was a retired executive with Chemical Bank. He had a Bachelor of Science degree from Fordham University's School of Business, a Juris Doctor from Fordham University, and had studied at Columbia University's Advance Management Program. *Id.*

The third arbitrator, Wayne Marsh, was a practicing attorney. He had a Bachelor of Science degree in Finance and Accounting from Arizona State University and Juris Doctor from Southwestern University School of Law in Los Angeles. *Id.*

C. The Arbitration Proceedings

On October 14, 1988, the McColloughs filed a Statement of Claim in letter form. Exhibit A to Defendants' Reply (E.R. 000238). This single-spaced three-page letter accused A.G. Edwards of a variety of items that were alleged in a perfunctory fashion. A.G. Edwards' fourteen affirmative defenses included contributory negligence and the applicability of the Arizona Consumer Fraud Act. Tab 13 to Motion to Vacate (E.R. 000059, 000065-000070). The McColloughs filed a twenty-five page brief, which specifically addressed A.G. Edwards' defenses regarding the Arizona Consumer Fraud Act and contributory negligence that were discussed by the District Court. Exhibit D to Statement of Facts (E.R. 000193-000195, 000203-000210).

The arbitrators heard testimony from nine witnesses, including expert testimony, during an eight-day proceeding. Exhibit A to Application to Confirm Arbitrators' Award (E.R. 000004-000005). The transcript from the proceeding exceeds 1,300 pages.

On October 2, 1990, the Arbitrators denied the McColloughs' claim and granted A.G. Edwards' counterclaim for $310,850.12 plus interest through October 1, 1990. The Arbitrators did not award attorneys' fees, costs, or expenses. *See* Appendix B.

D. The Arbitration Record

The McColloughs failed to prevail on securities fraud allegations in the N.Y.S.E. arbitration. McColloughs attempt to depict A.G. Edwards as wrongdoers by unsubstantiated statements of alleged misdeeds. Petition at 3,

19-20. The issues regarding alleged unauthorized trading, securities fraud and deceptive practices in the McColloughs' options accounts were before the Arbitrators through numerous factual and expert witnesses. These issues were highly disputed. The Arbitrators found in favor of A.G. Edwards.

Despite having no evidence, the McColloughs attempt to color the view of the Court by repeatedly insisting the Arbitrators' decision was "probably influenced" by affirmative defenses that A.G. Edwards raised. Petition at 6, 24-26. The McColloughs cannot cite to any part of the Record that shows such influence. The District Court made no such finding. Other than A.G. Edwards initially raising the defenses in response to the McColloughs' broad and indulgent Statement of Claim, the McColloughs have no basis in fact to assert their position. McColloughs' counsel thoroughly and specifically briefed and orally addressed the affirmative defenses that A.G. Edwards raised. The McColloughs failed to prove their case and have no basis to assert their current position.

Many factual scenarios fully justify the Arbitrators' decision to find in favor of A.G. Edwards. The risk assumption language in their Options Account Agreement indicated knowledge. The repetitious trading activity and documented confirmation of options trades indicated notice and understanding. The McColloughs were sophisticated investors and failed to prove their case under the applicable securities laws. After $160,000.00 of profiting by engaging in speculative trading, the McColloughs suffered the same unfortunate fate

as many investors who engaged in risky investment strategies because of the October 19, 1987, stock market crash. Transcript of Oral Argument at 25-26. The McColloughs' desire to eliminate the debit balance in their account over time when they signed a promissory note and release and commenced payments is consistent with the arbitration award.

The McColloughs voluntarily executed the promissory note and release. They imply they were misled into signing a note wholly foreign to them. Petition at 3-4. The McColloughs reviewed the note in private without the presence of any representatives of A.G. Edwards. Testimony of David Minnick, Ex. B to Statement of Facts (E.R. 000134-000138). After fully reviewing the note, the McColloughs requested a change to one paragraph of the note. *Id.* (E.R. 000136-000137); Promissory Note at 2, Application to Confirm Arbitrators' Award (E.R. 000013). These facts were presented to the Arbitrators.

E. Petitioners' Misstatement of the Law

The McColloughs assert the law requires a reasoned decision whenever a statutory claim is arbitrated to maintain at least "minimal integrity" in process. Petition at 6-7; *cf.* Petition at 15-21. Nothing in the law, the N.Y.S.E.'s procedures or the Federal Arbitration Act's legislative history requires a reasoned decision unless one is requested in a timely fashion. The McColloughs did not do so. Statement of Facts, ¶ 11 (E.R. 000116-000117); Ex. G to Statement of Facts (E.R. 000230).

1. A Reasoned Decision Was Not Requested

Prior to, during, and at the conclusion of the arbitration proceeding, the McColloughs did not request a reasoned decision or an opinion, even though the N.Y.S.E. Arbitration Procedures Manual authorizes a party to make such a request prior to the hearing date. *See* Appendix C. When the McColloughs requested an opinion after an unfavorable award, the N.Y.S.E. denied the request because it was untimely. Statement of Facts, ¶ 11 (E.R. 000116-000117); Ex. G to Statement of Facts (E.R. 000230).

2. No Fraud Or Misconduct Was Found

The District Court rejected the McColloughs' argument that A.G. Edwards' defenses constituted fraud. It recognized the McColloughs had to prove by clear and convincing evidence that any fraud must not have been discoverable upon the exercise of due diligence prior to or during the proceeding and that it was materially related to an issue in the decision. The District Court recognized that "all the alleged 'misstatements' were known to, and pointed out to the arbitrators by, Defendants' [McColloughs'] counsel." Memorandum and Order at 9 (E.R. 000249).

The District Court recognized that:

> . . . counsel for both parties presented their legal arguments in the usual adversarial way, both orally and through legal memoranda. Plaintiff [A.G. Edwards] submitted two briefs and Defendants [the McColloughs] at least one brief. Defendants' complaint might be considered simply as a difference of opinion on the law; that is,

> Defendants believe they should have won on the law.

Id. at 9-10 (E.R. 000249-000250).

The District Court did not find any causation between the award and the defenses; nor did it find the defenses were material or that A.G. Edwards had acted in bad faith.

3. Note and Release Defense Is Fact Intensive

The McColloughs misstate that the note and release defense was one of the defenses upon which the District Court vacated the arbitration award. Petition at 5-6, 23-25. The District Court only opined on two of the defenses – contributory negligence and Arizona Consumer Fraud Act. Memorandum and Order at 8-9 (E.R. 000249). The note and release legal defense is valid if supported by credible testimony. Under Arizona law, a release of legal claims is enforceable where there is a mutual agreement containing a release executed by the parties that is supported by consideration. *See, e.g., McGrath v. Bill Johnston Golf Properties, Inc.*, 13 Ariz. App. 49, 474 P.2d 56 (1970).

As a factual issue, this dispute went before the Arbitrators. The Arbitrators found against the McColloughs who testified they had executed and began making payments on the note and then defaulted.

The McColloughs attempted to expand this issue in their Answering Brief before the Ninth Circuit Court of Appeals ("Answering Brief") at 23. However, the McColloughs failed to cross-appeal to properly raise an

issue on the note and release defense. Memorandum and Order at 8-9 (E.R. 000249); *see* Fed. R. App. P. 4(a).

4. Dissenting Opinions Are Not The Law

The McColloughs inappropriately place great reliance on dissenting opinions, such as asserting that the view expressed by the *Wilko v. Swan* minority is now the law. *See* Petition at 7-15, 28-29 ("Now this Court has aligned itself with the Second Circuit's approach to *Wilko*"). The Petition ignores case law in this Court regarding the arbitration process, and law in various courts interpreting the Federal Arbitration Act as applied to this case by the Ninth Circuit. That law uniformly limits judicial review of arbitral decisions and does not permit courts to "presume" error in an arbitration award because it does not contain reasons.

REASONS FOR DENYING THE WRIT

I. SUMMARY OF ARGUMENT

This case raises a limited issue as to what constitutes "undue means" as used in Section 10(a)(1) of the Federal Arbitration Act[3] to justify vacating an award that is proper on its face. 9 U.S.C. §§ 1 *et seq.* Section 10(a)(1) authorizes vacatur only if "the award was produced by corruption, fraud, or undue means."

[3] Section 10(a) was amended in 1990. Section 10(a)(1) used to be Section 10(a). No substantive changes to Section 10(a) were made in the amendment.

A.G. Edwards raised two affirmative defenses in arbitration pleadings in response to a broad and indulgent Statement of Claim written in letter form, which asserted various state and federal statutory and common law arguments. The McColloughs addressed the defenses in briefs to the arbitration panel. No evidence was presented to the District Court that the Arbitrators relied upon or even considered the defenses in reaching their decision. The District Court made no finding of causation or bad faith in its decision. It found, instead, that merely raising the defenses constituted undue means.

The District Court vacated the award even though its own findings contradict a well-established test for vacatur under Section 10(a). The test for vacatur requires a finding by clear and convincing evidence that:

(1) The McColloughs did not know of the allegedly erroneous defenses during the arbitration; and

(2) The defenses materially related to an issue in the arbitration decision, *i.e.*, a causal connection to the award exists.

The Ninth Circuit Court of Appeals found the District Court had no authority for its conclusion and was in conflict with the law of the Circuit.

II. THIS DECISION IS NOT IN CONFLICT WITH DECISIONS OF OTHER CIRCUITS AND DOES NOT PRESENT A NOVEL QUESTION OF LAW

Pursuant to the Supreme Court Rules, Rule 10.1, special and important reasons do not justify granting a review on writ of certiorari here. At no place in the

McColloughs' Petition do they show that the Ninth Circuit's decision in this case is in conflict with the decisions of any other United States Court of Appeals on the same matter. *See* U.S. Supreme Ct. R. 10.1(a). The federal courts of appeal universally agree that arbitrators are not required under the Federal Arbitration Act, or by common law, to render a reasoned decision. *E.g., Fahnestock & Co., Inc. v. Waltman*, 935 F.2d 512, 516 (2d Cir. 1991) (employment arbitration); *Antwine v. Prudential Bache Securities, Inc.*, 899 F.2d 410, 412 (5th Cir. 1990) (securities arbitration).

The Ninth Circuit decision has not departed from the "accepted and usual course of judicial proceedings," such that this Court should exercise its power of supervision. *See* U.S. Supreme Ct. R. 10.1(a). The Ninth Circuit Court of Appeals expressly found that the District Court had exceeded its authority and departed from the federal courts' accepted and usual limited review of arbitration awards. *A.G. Edwards & Sons, Inc. v. McCollough*, 967 F.2d 1401, 1404 (9th Cir.), *petition for cert. filed*, No. 92-747 (Oct. 26, 1992) (same case under appeal by McColloughs' Petition).

The Ninth Circuit has not decided a novel question of federal law. U.S. Supreme Ct. R. 10.1(c). As McColloughs' Petition indicates, this Court has extensively examined the same issues present here. This Court has repeatedly upheld the principle that federal judicial review of arbitration awards is limited. *See, e.g., Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 232, 107 S. Ct. 2332, 2340 (1987). Moreover, this Court recognizes that "[a]rbitrators have no obligation to the court to give their reasons for an award." *Alexander v. Gardner-Denver Co.*, 415 U.S. 36,

58, 94 S. Ct. 1011, 1024 (1974) (quoting *United Steelworkers of Am. v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 598, 80 S. Ct. 1358, 1361 (1960)). The Ninth Circuit decision here does not conflict with the applicable decisions of this Court. *See* U.S. Supreme Ct. R. 10.1(c).

III. THE PETITIONERS' LEGAL POSITION IS CONTRARY TO THE FEDERAL ARBITRATION ACT

The McColloughs fail to demonstrate that "undue means" was the basis for the arbitration award.[4] The cornerstone of the McColloughs' Petition is that the existing state of the law is wrong and should be judicially changed. McColloughs are unhappy because a majority of the Arbitrators found against them on the facts.

A. Limited Judicial Review of Arbitration Decisions Is the Law Despite the Court's Overruling of *Wilko v. Swan*

The McColloughs have chosen their forum and litigated their substantive claims. *See Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477, 481, 109 S. Ct.

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[4] The trial judge stated little precedent existed in the entire country and none in the Ninth Circuit to determine what constitutes "undue means." Memorandum and Order at 12 (E.R. 000252). As cited in A.G. Edwards' Opening Brief for the Ninth Circuit Court of Appeals, and despite the District Court's assertion, the Ninth Circuit has considered the meaning of "undue means" as *deliberately disregarding* what the arbitrators know to be the law. Opening Brief at 13-14 (citing *San Martine Compania de Navegacion, S.A. v. Saguenay Terminals, Ltd.*, 293 F.2d 796, 801 (9th Cir. 1961)).

1917, 1920 (1989). The McColloughs misread the *Rodriguez de Quijas - McMahon - Mitsubishi* line of cases for the proposition that the Court now requires reasoned decisions for certain arbitration cases (cloaked in the language of "greater judicial review"). *Compare Id.; McMahon*, 482 U.S. at 232, 107 S. Ct. at 2340; *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 105 S. Ct. 3346 (1985).

The Court's overruling of *Wilko v. Swan*, 346 U.S. 427, 74 S. Ct. 182 (1953), does not result in the conclusion that an arbitration award without a statement of reasons violates the Federal Arbitration Act. The minority opinion contained several different propositions.

The main issue of *Wilko* was whether an agreement to arbitrate securities claims is enforceable. *Id.* at 430, 74 S. Ct. at 184. The Court held that "the right to select the judicial forum is the kind of 'provision' that cannot be waived under § 14 of the Securities Act." *Id.* at 435, 74 S. Ct. at 186. The majority then went on to find that, if a case is submitted to arbitration, power to vacate an award is limited. *Id.* at 436, 74 S. Ct. at 187. Only the non-waiver of forum selection holding of the *Wilko* decision was overruled. *Rodriguez de Quijas*, 490 U.S. at 479-82, 109 S. Ct. at 1919-20. A court's power to review arbitration awards is limited. *See Id.; McMahon*, 482 U.S. at 232, 107 S. Ct. at 2340.

The *Rodriguez de Quijas* Court expressly upheld the enforceability of pre-dispute arbitration agreements in federal securities-related claims. 490 U.S. at 479-81, 109 S. Ct. at 1919-20. This Court abandoned any notion that courts should be hostile to an arbitration proceeding. *Id.*

at 480, 109 S. Ct. at 1920. In overruling *Wilko*, the *Rodriguez de Quijas* Court stated:

> To the extent that *Wilko* rested on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants, it has fallen far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes.

Id. at 481, 109 S. Ct. at 1920.

B. Federal Policy Favors Arbitration

"The [Federal] Arbitration Act establishes a 'federal policy favoring arbitration.'" *McMahon*, 482 U.S. at 226, 107 S. Ct. at 2337. Nothing in the *Rodriguez de Quijas – McMahon – Mitsubishi* line of cases suggests that reasoned decisions are necessary to protect substantive rights in securities-related arbitration. Indeed, the Court in *Rodriguez de Quijas* found "the arbitration process does not inherently undermine *any* of the substantive rights afforded to petitioners under the Securities Act." 490 U.S. at 486, 109 S. Ct. at 1922 (emphasis added). The *McMahon* Court said that "we have concluded that the streamlined procedures of arbitration do not entail any consequential restriction on substantive rights." 482 U.S. at 232, 107 S. Ct. at 2340. Moreover, "agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute." *Mitsubishi*, 473 U.S. at 628, 105 S. Ct. at 3354; *accord, e.g., Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. ___, 111 S. Ct. 1647, 1652 (1991).

In McColloughs' case these substantive claims were vigorously litigated. The McColloughs failed to meet their burden of proof before the arbitration panel and have not met the requirements of 9 U.S.C. § 10(a)(1) to justify vacating the award.

> Sometime ago this Court expressed 'hope for [the Act's] usefulness both in controversies based on statutes or on standards otherwise created,' . . . , and we are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution.

Mitsubishi, 473 U.S. at 626-27, 105 S. Ct. at 3354 (citations omitted).

Recent federal courts of appeals decisions have upheld the federal policy favoring arbitration. *R.M. Perez & Associates, Inc. v. Welch*, 960 F.2d 534 (5th Cir. 1992), expresses the judicial deference that still prevails in federal courts. Absent a sound statutory basis, courts may not overturn an arbitrator's award. *Id.* at 540.

> Because of the speed and informality of arbitration proceedings, 'whatever indignation a reviewing court may experience in examining the record, it must resist the temptation to condemn imperfect proceedings without a sound

> statutory basis for doing so.' . . . *Forsythe International* binds us to review the plaintiffs' challenge solely for errors specified in § 10.

Id. (quoting *Forsythe Int'l, S.A. v. Gibbs Oil Co. of Texas*, 915 F.2d 1017, 1022 (5th Cir. 1990)). The McColloughs desire a less strict standard of judicial review. However, any expanding of judicial review would undermine the federal policy toward arbitration and open the floodgates to additional litigation. *Id.*

Similarly, in *O.R. Securities, Inc. v. Professional Planning Associates, Inc.*, the Eleventh Circuit Court of Appeals required some showing in the record, "other than the result obtained, that the arbitrators knew the law and expressly disregarded it." 857 F.2d 742, 747 (11th Cir. 1988). Failing to give a reasoned decision or opinion is not grounds for vacating an arbitration award. *Id; accord San Martine Compania de Navegacion*, 293 F.2d at 801 (undue means exists only if the arbitrators deliberately disregarded the law). No evidence exists that this occurred!

The *Rodriguez de Quijas – McMahon – Mitsubishi* line of cases affirm the Court's confidence toward arbitration in securities-related cases and mandates a plain reading of the Federal Arbitration Act, which only requires vacatur if the evidence shows the arbitrators decided a case based on fraud, undue means, or by exceeding their authority. 9 U.S.C. § 10(a).

C. Arbitration Awards Are Presumed Valid

In *Sargent v. Paine Webber Jackson & Curtis, Inc.*, the Court of Appeals explained more than a "mere possibility" of an error *must exist* and that an arbitration award without an explanation *did not justify* vacating the award. 882 F.2d 529, 532 (D.C. Cir. 1989). It also said that so long as "the record disclosed a permissible route to the stated conclusion," then a court *must* uphold the arbitration award. *Id.*; *see, e.g., Lenslite Co. v. Zocker*, 95 Ariz. 208, 388 P.2d 421 (1964) (presuming correctness of trial court decisions on appeal).

> Finally, we have indicated that there is no reason to assume at the outset that arbitrators will not follow the law; although judicial scrutiny is limited, such review is sufficient to ensure that arbitrators comply with the requirements of the statute.

McMahon, 482 U.S. at 232, 107 S. Ct. at 2340. Even when a party's claim is grounded on statutory rights, arbitration is valid and enforceable. *Id.* at 226, 107 S. Ct. at 2337. Courts presume an arbitration award is valid unless otherwise proven.

State trial court appeals in ordinary litigation provide an excellent analogy. When a trial court decides an issue but does not state its reasons, the court of appeals will presume the decision was correctly made. *Lenslite Co.*, 95 Ariz. at 216, 388 P.2d at 426; *Melton v. Lehmann*, 794 P.2d 650, 653 (Idaho Ct. App. 1990). To uphold that presumption, appellate courts will use any reasonable evidence in the record that might support the decision. *Myers-Leiber Sign Co. v. Weirich*, 2 Ariz. App. 534, 536, 410 P.2d 491, 493

(1966). This is true even though "substantive rights" have been litigated. *Cf.* Petition at 15. But appellate courts will *not* go beyond the record. *Myers-Leiber*, 2 Ariz. App. at 536, 410 P.2d at 493.

There are many permissible routes for the Arbitrators to have found in favor of A.G. Edwards. The McColloughs were sophisticated investors and failed to prove their case under the applicable securities laws. Transcript of Oral Argument at 25-26. The McColloughs desired to eliminate the debit balance in their account over time and signed a promissory note and commenced payments. The McColloughs' account records and option profits reflect an understanding of trading risks.

To overturn an arbitration award, proper on its face and with no facts to indicate the law was not applied correctly, invites courts to reject awards when they do not like or agree with an arbitration panel's decision. This will totally erode any certainty of an apparently valid award where only a small part of the arbitration record is reviewed. *See, e.g. Sargent*, 882 F.2d at 532.

When faced with a district court that had remanded an arbitrator's award for an explanation, the District of Columbia Circuit in *Sargent* expressly rejected expanding the law stating that:

> If courts required an explanation on account of the mere possibility of such an error, they would in effect be requiring an explanation almost universally. The Supreme Court has observed that arbitral awards may be made without explanation.

Id. (citing *Wilko v. Swan*, 346 U.S. 427, 74 S. Ct. 182, as still valid on that point of law).

The McColloughs assert that "strong public policy" requires arbitrators to decide cases "in accordance with applicable statutory law." Petition at 19-21. McColloughs have no evidence that legal error occurred. They ignore the legal presumption that arbitration awards are decided in accordance with applicable statutory law absent evidence to the contrary. A decision in one party's favor creates a presumption that the arbitrators found for that party on "every controverted fact." *Lenslite Co.*, 95 Ariz. at 216, 388 P.2d at 426.

Only when facts appear in the Record that make it "probable that the Arbitrators committed an error" is the District Court justified in vacating the award. *Sargent*, 882 F.2d at 532. The McColloughs failed to meet this burden of proving that the Arbitrators made their decision on invalid grounds. *See McMullin v. Palmer*, 40 F.R.D. 368, 372 (N.D. Miss. 1966); *Moran v. Pittsburgh-Des Moines Steel Co.*, 86 F. Supp. 255, 284 (W.D. Penn. 1949), *rev'd on other grounds*, 183 F.2d 467 (3d Cir. 1950).

To satisfy their burden of proof, McColloughs must prove by clear and convincing evidence that the alleged impropriety was the basis of the Arbitrators' decision. *LaFarge Conseils et Etudes, S.A. v. Kaiser Cement & Gypsum Corp.*, 791 F.2d 1334, 1339 (9th Cir. 1986). A "mere possibility of such an error" is not sufficient. *Sargent*, 882 F.2d at 532; *see Karppinen v. Karl Kiefer Machine Co.*, 187 F.2d 32, 35 (2d Cir. 1951).

D. McColloughs Seek Judicial Amendment to the Federal Arbitration Act

Congress must modify federal acts, not the courts. *See Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625, 98 S. Ct. 2010, 2015 (1978). The Federal Arbitration Act sets out the basis for vacatur of an arbitration award. 9 U.S.C. § 10(a). The McColloughs urge this Court, using a misapplication of the *Rodriguez de Quijas – McMahon – Mitsubishi* line of cases, to go beyond § 10(a) and second guess the Arbitrators due to the absence of a reasoned decision. Petition at 7-15. This requires that the law be changed. But only Congress can amend a federal enactment. *See Mobil Oil*, 436 U.S. at 625, 98 S. Ct. at 2015.

IV. THE ARBITRATION DECISION IS CONSISTENT WITH APPLICABLE LEGAL PRINCIPLES

A. McColloughs Had Adequate Opportunity to Protect Substantive Rights

The McColloughs argue for a reasoned decision because their account agreement did not require them to waive their substantive rights. They sarcastically set forth revised contract language at page 29 of their Petition indicating their unsupported theory that Arbitrators disregarded the law. Petition at 11, 15 (quoting *Rodriguez de Quijas*, 490 U.S. at 481, 109 S. Ct. at 1920), 16, 18. This argument fails for several reasons.

First, the McColloughs had the opportunity to counterclaim in federal court when A.G. Edwards filed the suit on their promissory note. *See* Fed. R. Civ. P. 13; Letter

to Lewis from Herf (E.R. 000144); Letter to Herf from Lewis (E.R. 000145). They chose to arbitrate instead.

Second, the McColloughs had the opportunity to request a reasoned decision prior to issuance of the award. *See* Statement of Facts, ¶11 (E.R. 000116-000117); Ex. G to Statement of Facts (E.R. 000230); Letter from Edward Morris, NYSE, to Lewis (E.R. 000101). They did not.

Third, they were represented by counsel who vigorously argued and briefed their factual and legal position. The McColloughs waived their right to request an opinion after the fact. *See Greenwell v. Spellman*, 110 Ariz. 192, 194, 516 P.2d 328, 330 (1973); Arbitration Procedures Manual at 16, Ex. G to Statement of Facts (E.R. 000227); Memorandum and Order at 13 (E.R. 000253). Now they are estopped from requesting greater judicial scrutiny. *Greenwell*, 110 Ariz. at 194, 516 P.2d at 330.

B. An Arbitration Award Need Not Contain Reasons

The securities industry arbitration rules do not require a reasoned decision. Nor are securities arbitrations "special cases."[5] *See* Petition at 16 n.4. The rules for "Arbitration Procedure" clearly state:

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[5] The McColloughs cite numerous lower court decisions for the proposition that "greater judicial scrutiny" is needed. Petition at 16-17 n.4. Again, the McColloughs simply misapply cases that have reversed arbitration awards for manifest legal error. For instance, the McColloughs cite *Allen v. Interinsurance Exch. of the Auto. Club of S. Cal.*, 80 Cal. Rptr. 247 (Ct. App. 1969), as requiring a court to review the arbitration decision for conformity with the rules of law. Petition at 17 n.4. However, in *Allen*,

> . . . Arbitrators are not required to write opinions or provide reasons for the award. A party, however, may request an opinion. *This request should be made no later than the hearing date.*

N.Y.S.E. Arbitration Procedures Manual at 16, Ex. G to Statement of Facts (E.R. 000227) (Appendix C) (emphasis added).[6] Arbitration Procedures Manual at 16, Ex. G to Statement of Facts (E.R. 000227); *see* 3A H. Bloomenthal, *Securities and Federal Corporate Law* § 8.30[2][f], at 8-154.21 (1991) ("award does not have to include a reasoned opinion").[7]

C. The "Record" Does Not Suggest Legal Error

1. Undue Means Was Not Proven as Matter of Law

Under federal law, "undue means" requires that the Arbitrators deliberately disregard what they know to be the law. *San Martine Compania de Navegacion*, 293 F.2d at 801. Section 10(a)(1), which authorizes vacatur if "the

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the findings and conclusions showed the erroneous application of law. *Allen*, 80 Cal. Rptr. at 250. The District Court before the Court here had no evidence in the Record nor any findings of the Arbitrators to conclude the Award was erroneous much less the result of undue means.

[6] The arbitration rules of the National Association of Securities Dealers ("NASD") also specify exactly what Arbitrators *must* include in an arbitration award, but the rules do not require a reasoned decision. Code of Arbitration Procedure, *NASD Manual* (CCH) ¶3741(e) (1992) (Appendix D).

[7] By analogy, Arizona does not require its state courts to give a reasoned decision except upon request before trial. Ariz. R. Civ. P. 52(a). Failure to request such findings acts as a waiver upon the parties. *E.g.*, *Greenwell*, 110 Ariz. at 194, 516 P.2d at 330.

award was procured by corruption, fraud, or undue means," requires that the party challenging the award prove:

(1) By clear and convincing evidence that the objectionable conduct was not known or discoverable upon the exercise of due diligence prior to the arbitration; and

(2) That the conduct related to a material issue in the arbitration.

LaFarge Conseils, 791 F.2d at 1339 (analyzing fraud); 9 U.S.C. § 10(a).

As the Ninth Circuit noted in 1961, "undue means" is found where the arbitrators know the law, but deliberately disregard it. *San Martine Compania de Navegacion*, 293 F.2d at 801. The meaning is evident in the underlying purpose of § 10(a), which shows Congress' desire to provide for an *impartial* arbitration. *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 147, 89 S. Ct. 337, 338 (1968). Undue means is to be construed with respect to conduct which could cause partiality, just like corruption (bribery) or fraud (lying). No instances of undue means, such as witness tampering, deliberately disregarding the law, partiality, bribery, *ex parte* contact, or dishonesty are even hinted in this proceeding, *i.e.*, no undue means was exerted by A.G. Edwards on any panel member.

In *Shearson Hayden Stone, Inc. v. Liang*, 493 F. Supp. 104 (N.D. Ill. 1980), the element of bad faith was mandated where the district court refused Shearson's request to vacate the award for undue means. The court stated:

> 'Undue means,' in the context of section 10(a) of the Act, has not been defined by the courts. The courts, however, appear to interpret 'undue means' in conjunction with terms 'corruption' and 'fraud' found in section 10(a) and thus *'undue means' requires some type of 'bad faith' in the procurement of the award.*

493 F. Supp. at 108 (emphasis added). In *Liang*, Liang instituted the arbitration proceeding when Shearson terminated his employment. *Id.* at 105. After the award was rendered in favor of Liang, Shearson learned that Liang had made misstatements on his employment application and sought to vacate the decision. *Id.* at 106.

The court rejected Shearson's claim of undue means because Shearson was unable to show it could not have discovered this evidence prior to the arbitration hearing. *Liang*, 493 F. Supp. at 109 (citing *Kirschner v. West Co.*, 247 F. Supp. 550, 553 (E.D. Pa. 1965) and *Karppinen v. Karl Kiefer Machine Co.*, 187 F. Supp. 32, 35 (2d Cir. 1951)). The Ninth Circuit has cited *Liang* with approval. *LaFarge Conseils*, 791 F.2d at 1339; *Dogherra v. Safeway Stores, Inc.*, 679 F.2d 1293, 1297 (9th Cir. 1982).

In *Forsythe International*, the Fifth Circuit reversed the district court's vacatur on fraudulent grounds alleging panel misconduct for refusing to hear material evidence. 915 F.2d at 1023. The Fifth Circuit found that the issue of discovery abuse was raised during the arbitration proceedings. The court deferred to the arbitrators' control of their own proceedings:

> Misconduct, even when deemed irrelevant to the merits, may nevertheless subject offenders to other sanctions. Arbitrators may, for example,

> devise appropriate sanctions for abuse of the arbitration process.

Id. at 1023 n.8.

In *Foster v. C.F. Turley*, 808 F.2d 38 (10th Cir. 1986), the Tenth Circuit remanded a vacatur where it was unclear if the fraud could have been discovered prior to the arbitration proceedings by exercising due diligence. *Id.* at 42. If the failure to disclose material facts could have been discovered, then vacatur would not be granted.

The Second Circuit has held that deliberately attempting to prejudice the panel did not constitute undue means, where the conduct was open, challenged by the opposing party, and the panel claimed it was not prejudiced. *Drayer v. Krasner*, 572 F.2d 348, 351 (2d Cir.), *cert. denied*, 436 U.S. 948 (1978).

Drayer involved a former registered representative who claimed undue means because the prevailing brokerage firm offered to the arbitrators a copy of an indictment by a federal grand jury of the registered representative, even though he had not been convicted. 572 F.2d at 351-52. Rejecting his contention, the court stated:

> The 'undue means' of (a), when read in conjunction with 'corruption' and 'fraud,' does not cover a case where a party openly offered evidence even for the sole purpose of causing prejudice, at least when, as here, the arbitrators declined to receive it and stated that they had not been prejudiced and would act only on the evidence before them. The experienced businessmen on the arbitration panel could surely be relied upon . . .

572 F.2d at 352 (footnote omitted).

In *Karppinen*, 187 F.2d at 35, an arbitration award was confirmed where the party seeking vacatur claimed the award was induced by perjured testimony. Assuming perjured testimony constituted fraud under Section 10(a), the court noted that,

> it necessarily raises the issues of credibility which have already been before the arbitrators once. . . . [T]herefore the party relying on it must first show that he cannot have discovered it during the arbitration, else he should have invoked it as a defense at that time.

187 F.2d at 35. The Second Circuit refused to vacate the award because the bearing of the issues before the arbitrators and that of the perjured testimony was "extremely remote . . . [a]nd cannot reasonably be thought to have affected their decision in determining any relevant questions before them. At most, it could only bear on a possible impeachment . . . as to collateral matters. . . . " *Id.* *Karppinen* was cited with approval in the Ninth Circuit decision *Dogherra*, 679 F.2d at 1297.

2. A Note And Release Is A Viable Legal Theory

The note and release defense was not found meritless by the District Court and involved vigorously disputed facts at the hearing. The legal defense is valid if supported by credible testimony. The defense is fact intensive. The Arbitrators had many facts before them in the multi-day proceeding.

Under Arizona law, a release of legal claims is enforceable. *See, e.g., McGrath*, 13 Ariz. App. 49, 474 P.2d 56. As

the McColloughs acknowledged in their Answering Brief, "waiver is a voluntary and an intentional relinquishment of a *known* right." Answering Brief at 23 (emphasis in original). This is a factual issue.

Release is valid on a federal securities-related claim if a person has knowledge of the claim. *Burgess v. Premier Corp.*, 727 F.2d 826, 831 (9th Cir. 1984). Knowledge is a fact question. The McColloughs, represented by attorneys at all stages of the arbitration, had full opportunity to present their factual evidence. These are factually disputed claims, which clearly provide an independent basis to sustain the award as the Arbitrators chose not to believe McColloughs' evidence.

V. CONCLUSION

The McColloughs' Petition for Writ of Certiorari must be rejected as the Ninth Circuit Court of Appeals correctly applied existing law, and its decision does not conflict with other circuits. There was no showing of undue means to justify vacating an arbitration award. Petitioners' arguments for the discretionary exercise of jurisdiction are those of a disappointed litigant who was unhappy that their case was rejected by a majority of a three-member arbitration panel. Special and important reasons contained in United States Supreme Court Rule 10.1(a) and (c) have not been met. The decision of the Ninth Circuit is not in conflict with another United States Circuit Court of Appeals on the same matter. There is no departure from accepted or usual course of judicial proceedings, no unsettled question of federal law and there

has been no decision rendered by the Ninth Circuit on a federal question that conflicts with any holdings of the U.S. Supreme Court.

A.G. Edwards requests that this Court deny the Petition for Writ of Certiorari and grant A.G. Edwards its attorneys' fees pursuant to the terms of the options account agreement and promissory note.

RESPECTFULLY SUBMITTED this 25th day of November, 1992.

CHARLES W. HERF
Counsel of Record
QUARLES & BRADY & FANNIN
One East Camelback
Suite 400
Phoenix, Arizona 85012
(602) 230-5500
Attorneys For Respondent

APPENDIX A

NEW YORK STOCK EXCHANGE UNIFORM SUBMISSION AGREEMENT

UNIFORM SUBMISSION AGREEMENT

Before the New York Stock Exchange

In the Matter of the Arbitration Between

Name of Claimant(s)

WILLIAM F. McCOLLOUGH

JEANENE McCOLLOUGH

and

Name of Respondent(s)

A.G. EDWARDS & SONS, INC.

GREG U. SMITH

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1. The undersigned parties hereby submit the present matter in controversy, as set forth in the attached statement of claim, answers and all related counterclaims and/or third-party claims which may be asserted, to arbitration in accordance with the Constitution, By-Laws, Rules, Regulations and/or Code of Arbitration Procedure of the sponsoring organization.

2. The undersigned parties hereby state that they have read the procedures and rules of the sponsoring organization relating to arbitration.

3. The undersigned parties agree that in the event a hearing is necessary, such hearing shall be held at a time and place as may be designated by the Director of Arbitration or the arbitrator(s). The undersigned parties further agree and understand that the arbitration will be conducted in accordance with the Constitution, By-Laws, Rules, Regulations and/or Code of Arbitration Procedure of the sponsoring organization.

4. The undersigned parties further agree to abide by and perform any award(s) rendered pursuant to this Submission Agreement and further agree that a judgement and any interest due thereon, may be entered upon such award(s) and, for these purposes, the undersigned parties hereby voluntarily consent to submit to the jurisdiction of any court of competent jurisdiction which may properly enter such judgment.

5. IN WITNESS WHEREOF, the parties hereto have signed and acknowledged the foregoing Submission Agreement.

CLAIMANT(S) SIGNATURE

/s/ William F. McCollough
WILLIAM F. McCOLLOUGH

/s/ Jeanene McCollough
JEANENE McCOLLOUGH

STATE OF ARIZONA)
: ss.:
COUNTY OF MARICOPA)

On the 14th day of October, 1988, before me personally appeared WILLIAM F. McCOLLOUGH and JEANENE

McCOLLOUGH to me known and known to me to be the person(s) who executed the foregoing instrument, and (they) acknowledged to me that (they) executed the same.

/s/ Karen L. Ingles
Notary Public

My Commission Expires April 10, 1992

RESPONDENT WILL EXECUTE A UNIFORM SUBMISSION AGREEMENT IDENTICAL TO THE UNIFORM SUBMISSION AGREEMENT EXECUTED BY CLAIMANT UFP

APPENDIX B

ARBITRATION AWARD

New York Stock Exchange
In the Matter of Arbitration Between NYSE

Case:

William F. McCollough and Jeanene McCollough vs. A.G. Edwards & Sons, Inc. and Greg U. Smith

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Date Filed: *11/10/88*
First Scheduled: *5/15/89*
Decided: Oct 2, 1990

Case Summary:*

Customers vs. Member Firm and Registered Rep alleging unsuitability, failure to disclose risks, failure to supervise, fraud and RICO violations.

10/1/90

Sessions: *(14)*
Discovery Conferences 4/10 & 5/14/90 (1&2), 7/17-20/90 (3-9), 9/20 & 21/90 (10-13)

Claim Data

Claim	$1,000,000+	CC 3rd Pty	$237,425.00
Punitive	*yes*	Punitive	*plus interest and expenses*
Atty Fees	*yes*	Atty Fees	*yes*
Deposit	*$1,000.00*	Deposit	

Award Data

Award	0	CC 3rd Pty	310,850.12 plus int.
Punitive	0	Punitive	0
Atty Fees	0	Atty Fees	0
Costs	*$6,750.00*	Costs	*$6,750.00*

Decision:* The undersigned arbitrators have decided and determined in full and final settlement of all claims between the parties that:

> Claimants' claim is denied and Respondent's counterclaim is granted in the amount of $310,850.12 which includes interest through October 1, 1990. Thereafter interest shall accrue at the rate stated on the promissory note until paid. Each party shall bear their own attorney's fees, costs and expenses.

Remarks:*

> Arbitrator Wayne P. Marsh disagrees with the majority and would grant Claimants' claim plus expenses and treble damages.

Arbitrators D = Dissents

WAYNE P. MARSH – Dissenting	/s/ Wayne P. Marsh Signature
J.W. PARKER	/s/ J.W. Parker Signature
CHARLES C. LEHING	/s/ Charles C. Lehing Signature

Phoenix	*AZ*	Oct. 2, 1990
City	State	Date

*Additional Pages May be Used if Necessary.

APPENDIX C

NEW YORK STOCK EXCHANGE ARBITRATION PROCEDURES MANUAL

Pages 15-16 of 20

HOW ARE THE PARTIES NOTIFIED OF THE ARBITRATORS' DECISION?

> When the arbitrators have reached their decision and have signed an award, copies will be mailed to the parties. The award will contain the names of the parties, a summary of the issues in controversy and the issues resolved, as well as the damages requested and awarded and the names of the arbitrators. The awards will be made publicly available. *Arbitrators are not required to write opinions or provide reasons for the award. A party, however, may request an opinion. This request should be made no later than the hearing date.* Some sponsoring organizations delete from the public version of awards information that identifies either the arbitrators or the parties. The decision of the arbitrators is final; that is, the decision is subject to review by a court only on a very limited basis.

(emphasis added).

APPENDIX D

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. MANUAL CODE OF ARBITRATION PROCEDURE

Pages 3723, 3724

INTERPRETATION OF CODE ¶ 3735

Sec. 35. The arbitrators shall be empowered to interpret and determine the applicability of all provisions under this Code [of Arbitration Procedure] which interpretation shall be final and binding upon the parties.

AWARDS ¶ 3741

Sec. 41 (a) All awards shall be in writing and signed by a majority of the arbitrators or in such manner as is required by applicable law. Such awards may be entered as a judgment in any court of competent jurisdiction.

(b) Unless the applicable law directs otherwise, all awards rendered pursuant to this Code shall be deemed final and not subject to review or appeal.

(c) The Director of Arbitration shall endeavor to serve a copy of the award: (i) by registered or certified mail upon all parties, or their counsel, at the address of record; or, (ii) by personally serving the award upon the parties; or, (iii) by filing or delivering the award in such a manner as may be authorized by law.

(d) The arbitrator(s) shall endeavor to render an award within thirty (30) business days from the date the record is closed.

(e) The award shall contain the names of the parties, the name of counsel, if any, a summary of the issues, including the type(s) of any security or product, in controversy, the damages and other relief requested, the damages and other relief awarded, a statement of any other issues resolved, the names of the arbitrators, the dates the claim was filed and the award rendered, the number and dates of hearing sessions, the location of the hearings, and the signatures of the arbitrators concurring in the award.

(f) All awards involving public customers and their contents, excluding the names of the arbitrators, shall be made publicly available. A party to an arbitration involving a public customer may request that the Director of Arbitration provide copies of all awards rendered by the arbitrator(s) chosen to decide its case. A party wishing to obtain such information must notify the Director of Arbitration with three (3) business days of receipt of notification of the identity of the person(s) named to the panel.

[Amended effective May 10, 1989; April 26, 1991; May 7, 1991; January 8, 1992]